

This letter discusses whether a piece of equipment qualifies for the graphic arts exemption. See 35 ILCS 120/2-5(4) and 35 ILCS 120/2-30. (This is a PLR).

September 29, 1999

Dear Mr. Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200, is in response to your letter of September 25, 1998. Review of your request for a Private Letter Ruling disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

This is a formal private letter ruling request made on behalf of COMPANY, under 2 Ill. Admin. Code ch. 1, sec. 1200.110. To the best of COMPANY's knowledge, the letter ruling requested herein is not (nor has it been) the subject of an audit, administrative or court case involving COMPANY or any related party.¹

FACTS

COMPANY is in the business of manufacturing and selling at retail machinery and equipment used in document printing and publishing, including a machine known as the MACHINE.

The MACHINE is used in the printing industry as an alternative to offset printing machinery. The MACHINE's technology, which combines high-resolution scanning or digital input and laser printing with flexible electronic storage and retrieval of 'digital masters,' allows for the printing of books at a significantly lower cost than is possible with offset printing. With the MACHINE, the first book produced will cost the same as the one-thousandth book. As a result, the MACHINE makes short run printing and printing on demand profitable for commercial printers.

MACHINE publishing systems can accept both paper and electronic documents as input. Documents may be inputted both by using a high resolution scanner that converts hardcopy originals to digital masters or by transmitting electronic files created by desktop publishing applications via a media or network server. After a document has been converted to digital form, the MACHINE's graphical user interface allows the

operator to specify job requirements, enhance images, change them and even create new documents, basically cutting and pasting electronically.

Once the digital master has been finalized, the operator creates a job ticket for printing. The printer produces up to 180 pages per minute at near off-set quality, 600 dot per inch ('dpi') resolution. To achieve this quality, the MACHINE printer uses a laser that burns the image to be printed onto a continuously used roller, which, after printing, is stripped clean of the image by a magnet. The document may be finished using MACHINE's binding capacity or may be bound using a printer's binding equipment. Attached is a brochure of the MACHINE 135 as it applies to Book Publishers.

RELEVANT AUTHORITY

Section 2-5(4) of the Illinois Retailers' Occupation Tax Act ('ROTA') exempts from tax:

Graphic arts machinery and equipment, including repair and replacement parts, both new and used, and including that manufactured on special order, certified by the purchaser to be used primarily for graphic arts production.

35 ILCS 120/2-5(4).

To qualify for the exemption, the machinery and equipment must be used primarily, over 50%, in graphic arts production. 86 Ill. Admin. Code § 130.325(c).

Graphic arts production means printing by one or more of the common processes or graphic arts production services as those processes and services are defined in Major Group 27 of the U.S. Standard Industrial Classification Manual. *Id.* § 130.325(b). Major Group 27 includes a variety of establishments engaged in printing by one or more common processes, such as letterpress, lithography (including offset), gravure, or screen, and also establishments that perform services for the printing trade, such as bookbinding and platemaking.

OPINION REQUESTED

COMPANY requests that the Department issue a Private Letter Ruling confirming that the MACHINE Publishing/Printing machine qualifies as exempt graphic arts equipment when used primarily in graphic arts production.

DISCUSSION

The MACHINE is exempt from sales tax pursuant to Section 2-5 of the ROTA because it is graphic arts machinery used primarily in printing, a service covered under Major Group 27 of the U.S. Standard Industrial Classification Manual. The MACHINE technology was developed to allow printers to capitalize on the demand for short supply

printing. The MACHINE performs the same functions as machinery used in an off-set print shop and the high quality output and finishing capacity of the MACHINE make the books produced by it indistinguishable from those prepared by off-set printing presses.

Once the document is converted into digital form, the MACHINE performs the functions of a laser printer. Moreover, after the image is in digital form, the operator can change the document, essentially electronically cutting and pasting. The image, when final, is printed by a mechanism that has a laser burning the image onto a roller, a process substantially similar to that of off-set printing. Unlike a photocopying machine, the MACHINE does not make a xerographic picture of a document on paper.² Rather, it is a technologically advanced publishing/printing machine developed to compete with offset print equipment.

While we recognize that the Illinois Department of Revenue in a Private Letter Ruling to COMPANY on September 11, 1991 discussed among other things, the tax treatment of a predecessor to the current models of the MACHINE, that ruling was somewhat simplistic and superficial. Moreover, even though the ruling noted that the Department has taken the position that photocopying machines do not qualify for the graphic arts machinery and equipment exemption, the MACHINE is not a photocopying machine.

Clearly, the Department's 1991 letter ruling seems to unfairly imply that any machinery manufactured by COMPANY is incapable of qualifying for the graphic arts machinery exemption. However, in our recent telephone conversations, you rejected such a proposition and emphasized that the Department will review the use of the machinery in question, not merely the label, when determining whether such machinery qualifies for the exemption. With this in mind, it must be noted that the Department has previously recognized that a 'laser printer could qualify for the [graphic arts] exemption if it is used in an exempt fashion.' Private Letter Ruling 87-0651 (Sept. 4, 1987).

As demonstrated by the facts above, the MACHINE publishing/printing machine is used in the same manner as machinery used in an off-set print shop and procedures almost identical output. Consequently, we respectfully request a letter ruling confirming that the MACHINE is exempt from sales tax as graphic arts machinery when primarily used in the graphic arts production process. If you intend upon ruling otherwise than as stated in this conclusion, we would like to schedule a meeting to discuss this matter.

As you have stated, the Retailers' Occupation Tax Act (ROTA) exempts from tax, "[g]raphic arts machinery and equipment, including repair and replacement parts, both new and used, and including that manufactured on special order, certified by the purchaser to be used primarily for graphic arts production." 35 ILCS 120/2-5(4). Until recently, graphic arts production was defined as "printing by one or more of the common processes or graphic arts production services as those processes and services are defined in Major Group 27 of the U.S. Standard Industrial Classification Manual." 35 ILCS 120/2-30. It has been the Department's practice to administer the exemption by looking at equipment and determining whether it falls within a printing process described in Major

Group 27. The types of printing that are referred to in Major Group 27 generally include traditional methods such as letterpress, lithography (including offset), gravure, or screen. However, printers have increasingly turned to high-tech computer-assisted printing processes and equipment that are nowhere described in Major Group 27. It is our opinion that the MACHINE publishing system is such an item.

Public Act 91-541 was signed into law on August 13, 1999. This measure amended the definition of "graphic arts production" to mean "printing, including ink jet printing, by one or more of the processes described in Groups 323110 through 323122 of Subsector 323, Groups 511110 through 511199 of Subsector 511, and Group 512230 of Subsector 512 of the North American Industry Classification System published by the U.S. Office of Management and Budget, 1997 edition. Graphic arts production does not include (i) the transfer of images onto paper or other tangible personal property by means of photocopying or (ii) final printed products in electronic or audio form, including the production of software or audio-books." It is the Department's opinion that printing by means of the MACHINE qualifies as graphic arts production under the new definition. Specifically, groups 323114 and 323115 of the North American Industry Classification System describe high tech quick printing and digital printing processes.

We believe, however, that the MACHINE does not qualify for the graphic arts exemption prior to the enactment of Public Act 91-541. It is not a process described in Major Group 27, and is therefore ineligible for the exemption. However, under the new statute, if the MACHINE is certified by the purchaser to be used primarily for graphic arts production, it qualifies for the exemption.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Martha Mote
Associate Counsel

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¹ While COMPANY is not a party to any audit involving the request made in this letter, COMPANY has been informed that one of its customers is being audited. However, it is unknown the full extent of the audit, except that a MACHINE printer was part of the equipment under audit.

¹ Webster's Third New International Dictionary defines 'xerography' as 'the formation of pictures or copies of graphic matter by the action of light on an electrically charged photoconductive insulating surface in which the latent image is developed with powers that adhere only to the areas formed by the powders, sometimes transferred to a sheet of paper.' Webster's 3rd New International 2644 (1986).